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C O N F I D E N T I A L SECTION 01 OF 02 REYKJAVIK 000279

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SUBJECT: Foreign Minister Assesses Icelandic Domestic and Foreign Policy Situations

Classified by: Ambassador Carol van Voorst for reasons 1.4 (b) and (d).

11. (U) At a November 28 lunch hosted by the Danish Ambassador, the dean of the diplomatic corps, Foreign Minister Gisladdottir told the assembled heads of mission she viewed Iceland's financial collapse as part of a global meltdown that must be resolved globally. In a pointed repudiation of the harsh comments of President Olafur Ragnar Grimsson at the same venue November 7, Gisladdottir stressed that the government of Iceland was extremely grateful to the IMF contributing members and the bilateral donors who were assisting Iceland to weather the ongoing economic crisis.

12. (C) Gisladdottir, who is the chair of the junior coalition party the Social Democratic Alliance (SDA), carefully noted that her party had not been in power during most of the time that the government and the banks were making the financial decisions which resulted in the crash this fall. The SDA therefore did not accept blame for bad government decisions or actions. However, she said that about half of the SDA ministers wanted to pull out of the coalition now because they felt the public was holding them responsible by association for mistakes made by the Independence Party. Repeating the line that she has consistently taken in public, Gisladdottir said that it would be irresponsible of the SDA to call for elections now, even though the party would undoubtedly come out very well in early elections. She believed it was necessary to put the IMF program into place and settle the 2009 budget before elections could be called. The government had serious business to complete over the next few weeks and should focus on the priorities to help citizens now crushed by financial debt and to prevent more businesses from going bankrupt. Gisladdottir did not rule out the possibility of elections next year. She said the government must respond to calls from the electorate for more transparency and an end to cronyism and privileged relationships between government and financial leaders. She noted that her party has called for the resignation of the Central Bank Board and other presumably responsible officials, but she refused to speculate as to why Prime Minister Haarde has not yet demanded their resignations.

13. (C) Although the MFA budget will be severely cut in 2009-10, Gisladdottir emphasized that Iceland's foreign policy has not changed.

The country appreciated its close and enduring ties to its Nordic brethren, to the U.S., and to newer friends such as India and China. There will be no changes in Iceland's approach to issues of particular concern, such as gender equality, the Middle East, human rights, Afghanistan, or peacekeeping and developmental aid, though budget strictures for the next few years will prevent Iceland from being as active as it has been or Gisladdottir would like it to be in these fields. Development aid, for instance, will of necessity be cut temporarily during what the experts predict will be two years of recession. Gisladdottir said that difficult political and financial choices needed to be made. She has been told to expect a very bad budget year in 2009, some easing of the situation in 2010, but no return to anything approximating what had been considered the "normal" status pre-crash until 2011 at the earliest.

14. (C) Asked what implications the budget cuts would have on Defense

Agency activities, Gisladdottir said there would be no change in security policy although some practical changes in operations would be necessary. The defense agreement with the U.S., and the security MOUs with Norway, Denmark, and Sweden would remain cornerstones of Iceland's foreign and security policy. It was not politically possible, however, to force through massive cuts in social welfare and education and not take equally drastic cuts in defense. Gisladdottir said that the government was asking NATO to reduce air policing deployments from four a year to three in 2009. The Defense Agency would be required to run its operations more cost effectively.

Several MFA projects would be put on ice: a concept paper evaluating trends in the High North, originally scheduled for release in December, would be postponed; the long-promised Threat Assessment paper will not be presented to the Althingi until the end of January at the earliest; and Gisladdottir would postpone as well her annual December wrap-up of foreign affairs developments for the Althingi.

¶5. (C) Turning to the EU, Gisladdottir reiterated her party's firm support for applying for membership as soon as possible, and said that the Independence Party congress scheduled for the end of January would be crucial in setting Iceland's future course as a country. She thought the Independence Party might well decide to approve a bid for membership at that meeting, although it was quite possible that the matter would split the party. The Progressive Party is also meeting in January on the same issue, and she thought a majority of that party would also approve a pro-EU platform. Some of the Left-Greens as well might be willing to put Iceland on the path for EU membership, but she wasn't confident that the party as a whole would change course in the foreseeable future. Gisladdottir didn't rule out the possibility of a major change in Iceland's political landscape, suggesting that the anti-EU faction of the Independence Party (whom she characterized as mostly the "old" party loyalists) could regroup with the anti-EU factions of the Left-Greens and the

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Progressive Party to form a new political entity.

¶6. (C) Gisladdottir predicted that Iceland would move ahead swiftly towards EU membership once the Independence Party decided to take action. An official application for EU membership would be followed by expeditious and presumably non-contentious negotiations in Brussels, then the Althingi would quickly enact the necessary legislation to change the constitutional language on sovereignty issues. A public referendum would settle the deal. Gisladdottir said she did not expect a referendum prior to a membership bid to determine whether or not Iceland should approach the EU for membership; she thought that the recent polls showing a clear majority in favor of membership were sufficient public approbation to get the process started. However, she thought it likely that the Progressive Party and the Left Greens would call for a pre-application referendum.

¶7. (C) When asked about MFA intentions to redress the damage caused to Iceland's international image by the economic crash, Gisladdottir said she was personally deeply distressed by the beating that the country had taken in the international arena. Press accounts of failed banks and feuding with friends were not good for Iceland's people or businesses. She hoped the country's traditional strengths would pull it out of the current image debacle: Iceland's broad and egalitarian society, its well-educated and disciplined workforce, and its geothermal expertise were enduring advantages deserving of international respect. She announced that the MFA's new Chief of Staff, Ambassador Kristin Arnadottir, had been tasked with the development of a campaign to project a more positive picture of Iceland overseas. The Foreign Minister herself plans to work towards this goal at the upcoming Helsinki OSCE ministerial and the Convention on Cluster Munitions signing ceremony in Oslo. (Note: The ForMin said she had not yet decided to attend the NATO ministerial in Brussels; although she gave no reason, we have been told by staff that her doctors want her to limit air travel for the time being.)

¶8. (C) Embassy Comment: This was Gisladdottir's first general meeting with the resident diplomatic corps since her brain surgery in September. She quickly put aside our concerns of surgery-related problems: although she said she did not yet have all her energy back, she appeared her normal self: decisive, analytical, humorous, gregarious, and clear-spoken. She spoke at length with only a few notes, using English that is even more idiomatic and practiced since her long involuntary sojourn in New York City. Gisladdottir is firmly

in control of her party and her ministry, so much so that the contrast between her situation and that of Prime Minister Haarde grows ever more striking. Her absence from Iceland during the bleak days of economic chaos in October, while unfortunate for the country itself, may prove to have been a political advantage to Gísladóttir herself by allowing the public to disassociate her and the SDA from the unpopular decisions taken during those contentious days. Since returning to Iceland, she has consistently and forcefully articulated the message that Iceland must honor its international obligations, take care of its people during the coming very hard times, and, to avoid any possibility of a repeat of the financial disaster, must join the European Union and adopt the euro as quickly as possible.

van Voorst